

03-0510  
Audit  
Signed 01/10/2005

BEFORE THE UTAH STATE TAX COMMISSION

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PETITIONER,	)	
	)	<b>ORDER</b>
Petitioner,	)	
	)	Appeal No. 03-0510
v.	)	Account No. #####
	)	Tax Type: Income Tax
AUDITING DIVISION OF THE	)	Tax Years: 1999 and 2000
UTAH STATE TAX COMMISSION,	)	
	)	Judge: Chapman
Respondent.	)	

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**Presiding:**

Kerry R. Chapman, Administrative Law Judge

**Appearances:**

For Petitioner: PETITIONER (by telephone)

For Respondent: RESPONDENT REPRESENTATIVE 1, Assistant Attorney General  
RESPONDENT REPRESENTATIVE 2, Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing pursuant to the provisions of Utah Code Ann. §59-1-502.5, on April 21, 2004. Petitioner is appealing an audit deficiency of additional Utah individual income tax and interest. Auditing Division ("Division") issued Statutory Notices of Audit Change on March 11, 2003 for the 1999 and 2000 tax years. The amount of additional tax assessed was \$\$\$\$\$\$ for the 1999 tax year and \$\$\$\$\$\$ for the 2000 tax year.

APPLICABLE LAW

Utah imposes income tax on individuals who are residents of the state, in Utah Code Ann. §59-10-104 as follows:

... a tax is imposed on the state taxable income, as defined in §59-10-112, of every resident individual...

"Resident individual" is defined in Utah Code Ann. §59-10-103(1)(p) as:

(i) an individual who is domiciled in this state for any period of time during the taxable year, but only for the duration of such period; or (ii) an individual who is not domiciled in this state but maintains a permanent place of abode in this state and spends in the aggregate 183 or more days of the taxable year in this state. For purposes of this Subsection (1)(p)(ii), a fraction of a calendar day shall be counted as a whole day.

State taxable income is defined in Utah Code Ann. §59-10-112 as follows:

"State taxable income" in the case of a resident individual means his federal taxable income (as defined by §59-10-111) with the modifications, subtractions, and adjustments provided in §59-10-114 . . .

Federal taxable income is defined in Utah Code Ann. §59-10-111 as follows:

"Federal taxable income" means taxable income as currently defined in Section 63, Internal Revenue Code of 1986.

Taxable income is defined in the Internal Revenue Code at 26 U.S.C. 63 as:

Except as provided in subsection (b), for purposes of this subtitle, the term "taxable income" means gross income minus the deductions allowed by this chapter (other than the standard deduction).

Gross income is defined in the Internal Revenue Code at 26 U.S.C. 61(a) as:

Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items: (1) Compensation for services, including fees, commissions, fringe benefits, and similar items; ...

The Utah Legislature has required that the taxpayer file an amended Utah return in the event the Internal Revenue Service adjusts the amount of federal taxable income in Utah Code Ann. §59-10-536(5) as follows:

- (a) If a change is made in a taxpayer's net income on his or her federal income tax return, either because the taxpayer has filed an amended return or because of an action by the federal government, the taxpayer must notify the commission within 90 days after the final determination of such change. The taxpayer shall file a copy of the amended federal return and an amended state return that conforms to the changes on the federal return. No notification is required of changes in the taxpayer's federal income tax return that do not affect state tax liability.
- (b) The commission may assess any deficiency in state income taxes within three years after such report or amended return was filed. The amount of such assessment of tax shall not exceed the amount of the increase in Utah tax attributable to such federal change or correction. The provision of this Subsection (b) does not affect the time within which or the amount for which an assessment may otherwise be made. However, if the taxpayer fails to report to the commission the correction specified in this Subsection (b) the assessment may be made at any time within six years after the date of said correction.

#### DISCUSSION

After receiving the Division's Statutory Notices, the Petitioner filed an appeal to contest the audit assessments. He subsequently retained an accountant to review his tax returns for 1999 and 2000, and pursuant to this review, the Petitioner filed federal and Utah amended tax returns for both the 1999 and 2000 tax years.

2000 Tax Year. The Internal Revenue Service ("IRS") reviewed the Petitioner's federal amended returns and accepted his 2000 amended return. The Division stated that the 2000 Utah amended return was consistent with the federal return he IRS accepted and, as a result, it accepted the 2000 Utah amended return and changed its records accordingly. As a result, the Division claimed that the 2000 audit assessment is no longer an issue. Based on the Division's

actions and recommendation, the Commission finds that the Petitioner's 2000 tax liability should be the amount reflected on his 2000 Utah amended return.

1999 Tax Year. The IRS, however, did not accept the changes made by the Petitioner on his 1999 federal amended return because, for federal purposes, the statute of limitations to make those changes had expired. The Division did not assert that the Petitioner's 1999 amended return would, in any way, violate Utah's statutes of limitations. The Division stated, however, that had the federal amended return been filed timely, it appears that the IRS would have accepted it because it is consistent with the 2000 amended return that it did accept. For this reason, the Division believes the 1999 Utah amended return is correct, as well.

However, because Utah law bases a Petitioner's Utah income tax liability on his or her "federal taxable income," the Division is reluctant to adjust the 1999 audit assessment to reflect the Petitioner's 1999 Utah amended return, even though it believes the return is correct. The Division stated that should its 1999 audit assessment be changed to reflect the tax liability shown on Petitioner's amended return, the amount of tax the Petitioner would owe for the 1999 tax year would decrease from \$\$\$\$\$ to \$\$\$\$\$, plus interest.

The Division explained that this situation presents it with a dilemma, whether to enforce an audit assessment that is consistent with the federal taxable income officially recognized by the IRS or to accept an amended return that it believes to be correct even though it reflects a different taxable income. The Division admitted that, in at least one situation, the Utah Supreme Court has ruled that assessment by the IRS is not a prerequisite for Utah to impose its tax liability. The Division stated that the Court issued this ruling in a case where the taxpayer filed both federal

Appeal No. 03-0510

and state returns on which he claimed \$\$\$\$ taxable income. Nevertheless, the Division requests the Commission disallow the Petitioner's 1999 Utah amended return because of the administrative problems that would occur if the IRS and the state have inconsistent positions on the Petitioner's "taxable income."

The Division did not argue that the Petitioner's 1999 Utah amended return should be disallowed for any other reason except that the "federal taxable income" reflected on it did not match the amount of taxable income officially recognized by the IRS and that such inconsistency would cause administrative problems. However, the Division provided no explanation of the administrative problems that would arise sufficient to outweigh the positive result achieved by imposing the correct tax liability. The Division does not question the accuracy of the 1999 Utah amended return, and there is precedent, for state purposes, for deviating from the "federal taxable income" actually recognized by the IRS. Nor does the Division present any argument that the 1999 Utah amended return would violate any statute of limitations. Under these limited circumstances, the Commission will accept the Petitioner's 1999 Utah amended return as an accurate reflection of his 1999 Utah tax liability. Accordingly, the Division is ordered to adjust its records to reflect the Petitioner's 1999 Utah amended return.

#### DECISION AND ORDER

Based on the foregoing, the Commission orders the Division to adjust its records to reflect the tax liability reflected on the Petitioner's Utah amended returns for both the 1999 and 2000 tax years. It is so ordered.

Appeal No. 03-0510

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission  
Appeals Division  
210 North 1950 West  
Salt Lake City, Utah 84134

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this \_\_\_\_\_ day of \_\_\_\_\_, 2005.

\_\_\_\_\_  
Kerry R. Chapman  
Administrative Law Judge

BY ORDER OF THE UTAH STATE TAX COMMISSION.

The Commission has reviewed this case and the undersigned concur in this decision.

DATED this \_\_\_\_\_ day of \_\_\_\_\_, 2005.

Pam Hendrickson  
Commission Chair

R. Bruce Johnson  
Commissioner

Palmer DePaulis  
Commissioner

Marc B. Johnson  
Commissioner

Appeal No. 03-0510

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